

Professional and Business Services:

A 2020 Vision for Growth



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The New Industry New Jobs Strategy is being implemented working closely with the Devolved Administrations in Northern Ireland, Scotland and Wales, recognising their particular and varying responsibilities. While many of the challenges facing professional and business services are common across the four countries of the United Kingdom some of the policies covered in this report are specific to England. The Devolved Administrations will consider the most appropriate arrangements in those areas for which they have devolved responsibility, to address the issues in ways that meet their circumstances.

Ministerial Foreword



The UK is a global leader in the supply of professional and business services. However, the recent financial crisis, the rapid growth of emerging economies, developments in technology and societal concerns about climate change and sustainability are changing the face of business across the globe.

This interim report is part of a series of reports examining key sectors of the economy under the Government's Growth Agenda. It seeks to establish the key priorities for government action that will help to ensure the UK professional and business sectors' future competitiveness over the next 5-10 years.

Accounting for almost 20% of national output and, 14% of UK exports Professional and Business Services are significant in their own right as well as being a bellwether for the economy more generally. Through their intimate links with the rest of the economy, business services are also a vector for good practice, innovation and change management, which in turn will promote the development of new business models and increase overall business competitiveness. They also support change in public service delivery. So it is therefore of the utmost importance that we in Government continue to work closely with service providers to improve procurement processes on the lines set out in the Public Services Industry Review.

We have worked with professional and trade bodies, and with the business community directly, to produce this report, complemented by input from the Research Councils, the Technology Strategy Board, the Regional Development Agency network, and academia. In particular, we ran a series of workshops with leading companies, taking "deep dives" into the main drivers of change up to 2020. We have synthesised the findings from the workshops and also benefited from the input of the Professional and Business Services Group, Chaired by Sir Michael Snyder.

I am grateful for the efforts of all those who have contributed. By sharing their perspectives and experience, they have ensured that Government policy to support the sector will be better informed. I look forward to receiving feedback on this report and delivering on the findings.

A handwritten signature in black ink that reads "L. Mervyn Davies". The signature is written in a cursive, slightly stylized font.

Lord Davies of Abersoch

UK Trade and Investment Minister.

1: Introduction

1.1 The professional and business services sectors comprise a wide range of activities and, over recent years, this sector has been the area of the UK economy where growth has been greatest, as illustrated in Figure 1 below.

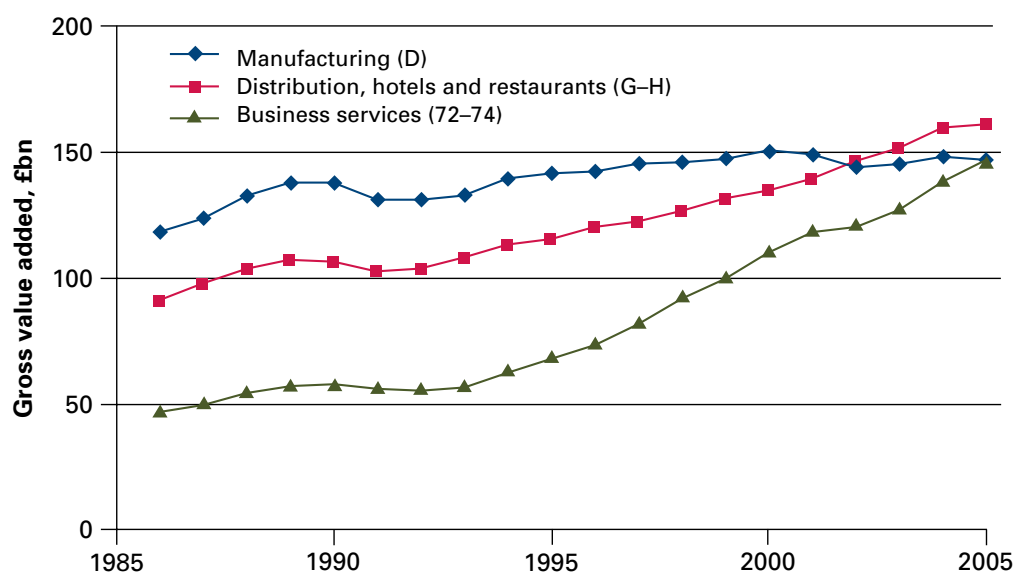
1.2 The overall professional and business services sector now accounts for almost 20% in terms of both national output (GVA) and employment. This report focuses more narrowly on legal, accountancy, advertising, ICT/digital content services, telecommunications and management consultancy. The rationale for this grouping is that it represents a key set of services which constitutes an “eco system” of services

that are high value, tradable and pervasive across the real economy.¹ As highlighted in Table 1, this grouping accounts for 12.9% by GVA and over 13.7 % of UK employment.

1.3 The statistics demonstrate that the professional and business service sectors’ contribution to output and employment is significant in its own right but its importance goes well beyond this.

1.4 With particular regard to the grouping of professional and business services, chosen for analysis in this report, the UK has world leading breadth and depth of capability which

Figure 1 The growth of business services 1985 – 2005



Source: Constant price output indices, 2003 prices, ONS.

¹ Construction related services such as architecture and financial services are being considered as part of other focused government work which includes the Innovation and Growth Team review of construction led by the chief construction advisor and the Reforming Financial Markets White Paper published in July 2009.

Table 1 Size and composition of the professional and business services sector

SIC	Sector	GVA		Employment	
		£Value (billion)	Share	No.	Share
63	Ancillary Transport Activities	21.7	1.8%	484	1.6%
64.1	Postal and courier services	9.0	0.7%	302	1.0%
64.2	Telecommunications	23.5	1.9%	223	0.7%
71	Renting of machinery etc	12.5	1.0%	167	0.5%
72	Computer services	37.5	3.0%	651	2.1%
73	Research and development	5.2	0.4%	120	0.4%
74.11	Legal activities	18.3	1.5%	368	1.2%
74.12	Accountancy services	13.3	1.1%	356	1.1%
74.13 to 74.15	Market research, management consultancy	16.9	1.4%	569	1.8%
74.2 + 74.3	Architectural activities & Tech. Consult	22.8	1.8%	507	1.6%
74.4	Advertising	6.4	0.5%	102	0.3%
74.5 to 74.8	Other business services	4.3	3.5%	2,126	6.8%
	Business Services (Total)	231.3	18.6%	5,974	19.2%

Value: £billion; employment in thousands.

Source: ONS Supply and Use Tables, Economic and Labour Market Review. All data are for 2007. GVA Share is relative to Whole Economy.

allows clients to tap into individual or combined expertise, in order to meet particular needs or solve specific problems. Moreover, the UK provides access to world class academic research and financial services for projects which need the benefit of deeper research, funding or insurance of whatever size and complexity.

1.5 This cluster of activity is particularly strong in London and the SE, which accounts for a very high proportion of UK trade in professional and business services as table 2 illustrates. However, this report also considers the role that other regions are playing in ensuring that the UK strength in professional and business services remains, not only globally competitive, but also

maximises its ability to support businesses in the wider UK economy.²

1.6 The growth of professional and business services has gone hand in hand with growth in the UK and global economy. However, events in the latter part of 2008 resulted in a considerable weakening of the financial services sector followed by a sharp reduction in economic activity. The world economy is only just emerging from the downturn. Unsurprisingly, the fortunes of business service firms such as in advertising have broadly reflected those of the wider economy, as illustrated in Figure 2 below, which

² The UK's expertise in high value services is in demand the world over. This being the case it is perhaps surprising that research conducted in 2005 by Woelfl found that the UK's manufacturing goods embody proportionately less service sector value added than manufactured goods of other OECD countries, including the US, France and Germany. In addition a DTI report also in 2005 found that over half of UK firms have reported that design has no role or only a limited role to play in their business.

Table 2. Regional value¹ of exports of selected services (current prices), 2007

£ million

ONS Pink Book Services Product Category	Government Office Region (GOR)										Rest of UK	UK
	North East	North West	Yorkshire and the Humber	East Midlands	West Midlands	Eastern	London	South East	South West			
Table 3.4 Communications Services	*	30	10	*	80	230	2,275	1,465	55	105	4,260	
Table 3.7 Computer and Information	45	130	105	55	145	525	2,645	3,115	110	205	7,080	
Table 3.8 Royalties and Licence Fees (part ²)	*	620	65	225	75	335	1,385	2,525	*	145	6,260	
Table 3.9 Other Business services (part ³) Merchandising and other trade related services	25	195	40	40	50	55	2,060	320	20	95	2,900	
Legal and accounting	20	*	35	*	50	55	3,420	180	60	125	4,420	
Business management and management consulting	130	205	115	50	125	275	3,395	1,035	355	320	6,005	
Advertising and Market Research	5	45	45	10	60	60	1,775	305	25	40	2,370	
Research and development	95	665	110	345	45	1,330	450	1,650	165	350	5,205	
Architectural, surveying and construction ⁴	20	75	70	80	25	70	300	460	20	255	1,375	
Engineering and technical services ⁵	180	260	75	125	45	560	1,635	1,685	215	700	5,480	
Services between affiliated enterprises, n.i.e.	40	135	40	70	80	285	1,690	870	115	300	3,625	
Services not Regionalised											101,665	
Total UK Exports of services											150,645	

1 Figures are not National Statistics and may not be accurate to the level shown. Regional data and UK totals are rounded to the nearest £5 million and are adjusted to be consistent with Tables 3.1

2 Excluding Film and Television Royalties and License fees, see Table 3.8 in the ONS Pink Book.

3 Excluding Other Miscellaneous Business services, see Table 3.9 in the ONS Pink Book

4 Construction figures from Table 3.1 in the Pink Book have been combined with figures for Architectural and Surveying from Table 3.9.

5 Also includes Operational leasing and Agricultural, mining and on-site processing

* Disclosive data, not available

Services not regionalised include travel, transportation and financial services.

Source: BIS analysis of the ONS International Trade in Services (ITIS) Inquiry

shows the change in marketing budget relative to GDP.

1.7 The Government recognised the risk which the decline in financial services activity posed to professional services and appointed a Group, drawn from a wide range of professional service firms and Government Departments, under the joint Chairmanship of Sir Michael Snyder and Lord Myners, to examine the challenges and opportunities facing the sector. The Group reported in March 2009 and recommended a single point of contact for professional services in Whitehall. In response to the report, the Department for Business has established a Services Policy Unit to act as a point of contact and, in preparing this interim report, the Unit has sought to build on the earlier work and to develop a strategy to promote innovation and growth in the broader business services sector.

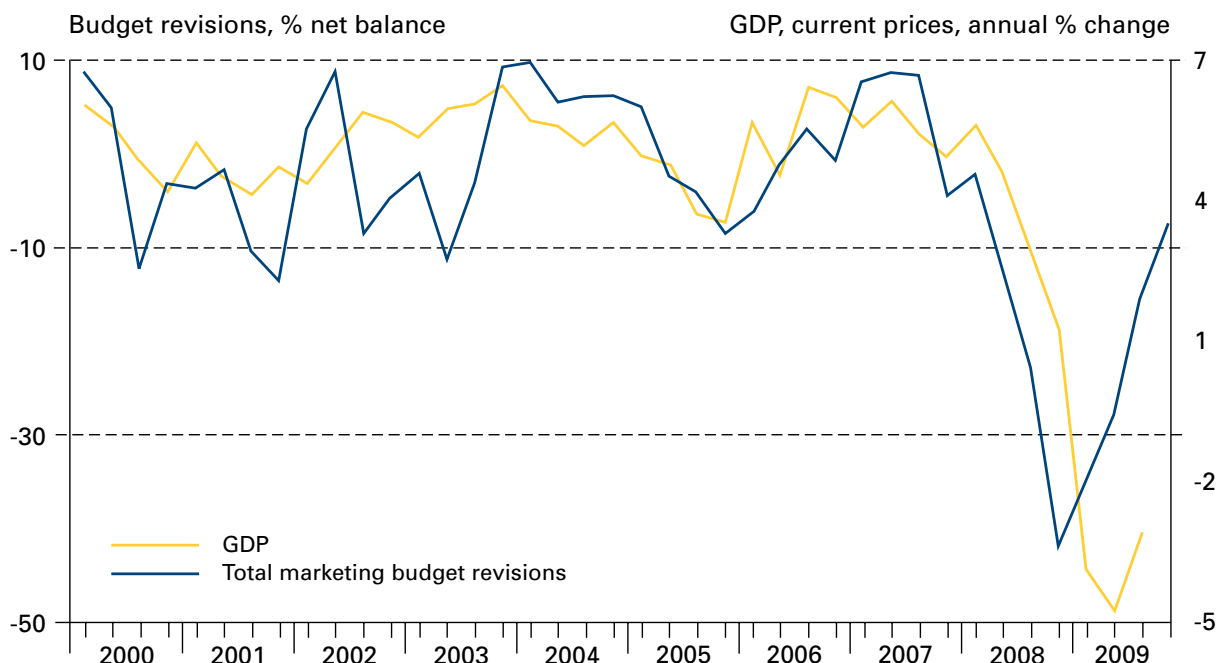
1.8 While the latest output statistics and purchasing manager indices for both manufacturing and service sectors are beginning

to show signs of recovery, it is clear that the business world is changing rapidly. To compete effectively, both business and Government policies need to respond to the new challenges to consolidate the UK's position and to maximise opportunities where growth will be significant.

1.9 Our consultation with business has confirmed that there are three main socio-economic drivers that have particular relevance to professional and business services, and these will intensify over the next decade:

- The further miniaturisation and ubiquity of computing, together with an improved communications infrastructure (mobile and "hard wired") will continue to impact on consumer behaviour and business models;
- Concerns about climate change and sustainability, which were not allayed by the Copenhagen Summit; and

Figure 2 Advertising and Marketing budgets and GDP



Source: Institute of Practitioners in Advertising

- Global GDP shift to emerging economies, which will bring both new markets and increased competition.

1.10 These drivers are considered in the next three chapters. The final chapter then considers the overarching or horizontal policy measures that Government is using to strengthen the overall business environment for professional and business services, which will in turn drive competitiveness and performance in the wider economy.

2: A networked world

2.1 The UK information and communication technologies sector (ICT) generated some £96 billion in gross value added and employed some 1.2 million people in 2007.³ However, the importance of ICT stretches even further as it is a key enabler of business services and financial services which, together, accounted for nearly a third of total gross value added and more than a fifth of total employment in 2007.

2.2 Predicted growth rates by E-skills UK suggested that employment growth in IT and telecoms professional occupations could rise by an average of 1.2% per annum between 2009 and 2018, leading to a net increase in employment of 128,000 over this period⁴.

2.3 In terms of future opportunities, our consultation with business has confirmed that four trends are already evident:

- The effective acquisition, analysis and use of information has become a key determinant of business performance.
- ICT is moving from an investment model, in hardware and software, to a utility model where access to business management information and communications is available as a service, 24/7, for a monthly fee. This is

dramatically reducing the cost of start-up for companies and enables rapid scalability as business grows.

- Amongst the younger generation, particularly the Y Generation,⁵ multitasking on a range of platforms and channels has become the norm, and remote social networks the medium for exchanging and validating information. Businesses are increasingly using “crowd sourcing” and co-creation techniques to develop new or improved services but a key question is how to monetise innovation and generate sustainable business models based on digital content.
- Advances in mobile communications technology are enabling innovation in a wide range of applications in both developed and developing countries. The latter are no longer constrained by the lack of a communications infrastructure and this is opening up new markets.

Business priorities: barriers to growth

2.4 While the business community recognises the progress being made by the Digital Britain report and its implementation, our consultation with the business community suggests the following priorities for a strategy up to 2020:

3 ICT estimates of gross value added and employment are BIS estimates based on the OECD definition of the ICT sector and calculated using ONS official statistics.

4 E-skills UK (2010) Technology Counts: IT and Telecoms Insights 2010

5 Y Generation broadly defined as those born between 1979-1991 and “natives” of the internet

ICT infrastructure

2.5 For the UK to remain competitive in a modern, and increasingly global, service oriented economy, business feels that the UK needs to match the aspirations of countries as far afield as Finland, Korea and China. Business believes that, to do so, will require focus on the mobile infrastructure as well as fixed line connections. In particular, it considers that the cost of current high speed connections is uneconomical for many SMEs and that, to be future proof to 2020, high speed connection needs to be around the 100Mbps mark. It therefore wishes to see Government articulate an ambitious vision for the ICT infrastructure to significantly improve effective broadband coverage outside the main conurbations.

Data protection and trust

2.6 While the Y Generation seems more open in giving access to their personal details and how they are used, our consultation with business indicated that there is a general concern about the provenance of information, issues of ownership and the potential for abuse. Organisations have access to a wide range of personal information eg, buying habits, daily travel arrangements, healthcare records, smart metering and public engagements and it is in business interests that consumer trust in e-commerce is maintained.

2.7 Business feels that Government has an important role in establishing a framework regarding ownership of personal data and the contractual arrangements relating to how it might be used. By so doing, it would also allay concerns regarding the relationship between personal information and the state. This could also lead to the development of new services

related to personal information in the form of trusted third parties, who would act as intermediaries between the individual and other parties.

Intellectual property and micropayments

2.8 Business believes Government has a key role in developing an IPR framework that strikes the right balance between the interests of the content creator and the consumer. But business also considers that Government could support such a framework by encouraging the development and deployment of payment systems for small transactions.

Public service information

2.9 The recent initiative to make public data available in a re-usable format is welcomed and business wanted Government to maintain the momentum of the Making Public Data Public project at national and local level. The project is important for the development of vibrant business information services across a wide range of activities where Government holds important datasets. For example, business believes that, if Government wishes business and society at large to begin to adapt to the prospect of climate change and risks to sustainability, then provision of data on flooding, weather and waste in linked and re-usable format would provide the necessary information to inform debate and decision making.

2.10 More generally our consultation indicates that, to help generate new services, business needs more transactional datasets to be released with a commitment to maintain the quality of data and the frequency of its release.

UK strengths in technology and application

2.11 The UK has world-class capability in the new emerging technologies, particularly those related to the web, and also in high value service applications. Business considers that policy should seek to harness the former to strengthen UK capability in the latter. For example:

- The increasing sophistication of data mining and analytics has the capacity to transform professional services, such as legal services and accountancy, as well as enable more targeted offerings by a wide range of service providers;
- Business services could be considerably enhanced by interface design and automatic translation;
- A variety of technologies could be brought to bear on improving identification, reducing fraud and thereby providing security for financial transactions regardless of size;
- UK excellence in education and training could be further strengthened by technology used in the UK's world-class computer games industry.

Skills

2.12 But technology itself is not enough. To retain its pre-eminence in high value services, which capitalise on the innovative application of ICT, the UK needs to ensure that business has a supply of graduates with, not only excellent computing skills, but also the ability to relate quickly to business processes and business applications. The USA is responding to the challenge of global competition by focusing on such skill-sets, and business believes that the UK should do likewise. However, digital content

providers argue that this should not come at the expense of creativity.

Government strategy

2.13 The Government agrees that ICT infrastructure and services are vital for the nation's competitiveness. To help British business capitalise on these trends, Government developed and published its strategy for Digital Britain around three main themes: infrastructure, content and participation.

2.14 We particularly agree that the UK's medium term competitiveness will be greatly influenced by the bandwidth available to consumers and businesses. We are committed to delivering a basic universal service, but believe action is also needed to deliver Next Generation, superfast broadband access to a much wider proportion of the country than the market will allow unaided. Following the Digital Britain White Paper, we have moved to establish a Next Generation Fund and have issued a consultation document that sets out the criteria by which NGA will be judged⁶. The NGA fund will support the market to deliver beyond the commercially attractive areas to at least 90% of the UK by 2017. We will bring proposals before Parliament in 2010 to establish the fund through a modest duty on landlines.

2.15 The Digital Britain White Paper also acknowledged the need to establish systems for small payments for online services and content, and committed the Technology Strategy Board to exploring through its Digital Test Beds new monetisation methods for online content,

⁶ Faster, more symmetrical download and upload speeds; greater reliability and consistency of service across users and over time; can include Fibre to Cabinet, Fibre to Home, satellite or mobile wireless technologies.

such as on demand video and music, through micropayments, embedded or personalised advertising or other means.

2.16 To support the strategy for Digital Britain, the Technology Strategy Board has allocated £30m to stimulate innovation in business modelling, technology and services. It will work alongside partners including businesses, Research Councils, Regional Development Agencies, NESTA and other Government bodies to invest in strategic programmes. The Technology Strategy Board has identified three challenges facing the market; the economics of the network and of content; user protection; and enablement.

Priority action for Government

Infrastructure: Work with the professional and business services sector to ensure the NGA consultation process takes account of the issues raised in this report.

Market framework: Government will continue to strengthen trust in the internet and develop an IP regime which strikes the right balance between owners and users. It will use TSB test beds to trial solutions around data protection, trust, intellectual property and micro payments.

Capability: Government will evaluate its pilot programme support of transformative ICT to determine the most effective means of support for business. It will explore with business the opportunities around making public data available to facilitate innovation and the development of new services and promote the next phase of web development. *Higher Ambitions*, the Government's higher education framework, will deliver further skills needed for new industry and new jobs, notably in STEM subjects. This includes £20m to support the goal of attracting students to STEM subjects in higher education.

3: A low carbon, sustainable economy

3.1 Notwithstanding the outcome of the Copenhagen summit, our consultation with business has emphasised the importance of sustainability and the response to climate change as key drivers of change in markets for business and professional services over the decade ahead. Business considers that the threat of price spikes for energy and key raw materials, the rapid decline in the number of landfill sites available and growing societal pressures make change inevitable.

3.2 Business services are *informing, catalysing and enabling* transition to a low carbon, resource efficient UK economy. Services and manufacturing are now enmeshed in the real economy, and service solutions are the mode of delivery, for example, for green/clean technologies. There is strong potential for further growth. The value of the UK low carbon environmental goods and services activities, defined broadly⁷, was estimated at £112 billion in 2008-09⁸, potentially growing at just under 4% per annum by 2015/16, and employing over 900,000, potentially rising to a million by mid-decade. The wider global market opportunity was estimated at £3.2 trillion in 2008-09, forecast to grow at 4% over the next five years. In addition, the UK, especially London, is a

global hub for the international carbon market, which has grown in recent years, driven by the frameworks of the EU Emissions Trading Scheme and the Kyoto Protocol – Section 4.0 addresses this further.

3.3 The business view is that low carbon and optimised resource management would, in the long term, be internalised by businesses as part of “business as usual”, but there is significant growth potential for business services in this area to 2020. Business emphasised that, fundamentally, cost reduction would remain a critical factor driving businesses towards more efficient, sustainable modes of operation, and would provide opportunities for services.

Areas of future growth

3.4 Our consultation with business identified the following areas of growth:

- A market price of carbon, *once high enough*, would provide a clear market signal to incentivise behavioural change across business and unlock myriad associated opportunities for business and professional services.
- Carbon reporting will generate a range of advisory, technical, legal, accountancy services; plus cross-disciplinary service opportunities.

⁷ Low carbon goods and services are a dynamic and growing spectrum of business activities and, by definition, hard to define. Business services, form part of this activity, but (i) the delivery of services and goods is sometimes inextricable and (ii) they extend across and is assimilated in the operation of business more generally.

⁸ “Low carbon environmental goods and services: an industry analysis. Update for 2008-09”, Innovas for BIS, 2010

- Existing patterns of resource and waste management in the UK economy are unsustainable and provide economic incentives for businesses to improve efficiency, to limit exposure to materials insecurity, and to exploit value opportunities from resource management.
- Businesses will be under pressure to prevent and control their pollution and environmental impacts, other than carbon emissions.
- The international market provides an opportunity for UK providers of business services to compete to deliver user-orientated services to the fast growing markets in major emerging global economies. There are strong UK capabilities in integrated service solutions and complex project management.
- Technology enables growth of low carbon and sustainability services, e.g. in measurement and monitoring of energy use and emissions.
- There is significant scope to make the modes of delivery of the general spread of business and professional services more sustainable, for example in using technology to avoid travel emissions; and in assessing the sometimes “hidden environmental footprint” of new services.

Business priorities for Government – establishing the right market framework

3.5 Our consultation with business told us that they see a need for Government to follow up its long-term policy direction with clear, cohesive policy delivery and in particular, *to take further steps to set a more favourable market framework for business investment.*

Infrastructure

3.6 Infrastructure is a prerequisite for a low carbon, resource efficient economy, e.g. decentralised electricity generation or materials reprocessing facilities, which unleashes a range of associated business services to optimise resource use. The business view is that Government could do more to set a favourable framework for private investment in infrastructure, which is often on a regional scale rather than local⁹. Government could act as a “convenor” to encourage the new economic partnerships and materials supply relationships needed at regional and sub-regional level to underpin infrastructure and to take a strategic approach to planning control, working with local authorities. The Regional Development Agencies are already active in varying ways¹⁰, and a new approach to these issues at regional level would address a key spatial aspect of the transition to the new economy.

Standards and information

3.7 Business feels Government should lead the establishment of a market framework of standards for a low carbon, resource efficient economy. This would help set the definitions and language through which business can address carbon and resource management; establish a framework for measuring and reporting; develop a means to denominate energy and resource efficiency in terms of carbon savings; and to calibrate and assess relevant business services and the value propositions they offer to users. Such a comprehensive framework required

⁹ Many of the projects at issue here fall below the thresholds for adjudication by the Infrastructure Planning Commission, <http://infrastructure.independent.gov.uk/>

¹⁰ For example, the Landfill Diversion Strategy “resource route map” location tool which is being piloted by Advantage West Midlands, <http://www.advantagewm.co.uk/news-media-events/news/2009/10/awms-landfill-diversion-strategy-identifies-opportunities-for-waste-investment.aspx>

Government to lead, working with BSI British Standards and other key players¹¹, including European and other international standards bodies given the global nature of supply chains. Moreover, standards development needs to be complemented with a clear communication strategy, disseminating the benefits of low carbon and resource efficiency in terms of costs and business value

Skills

3.8 Business underlined the need for a framework of skills development to support a framework for a low carbon, resource efficient economy. The challenge lay in the prospect of demand for some skills sets only surfacing strongly during the course of the next decade. Accountants and lawyers commented on their needs to develop new skills to respond to market demands for carbon reporting and referred to the role of standards in this context.

Government strategy

3.9 The Government has set out, in its Low Carbon Industrial Strategy,¹² a programme of actions and support for businesses moving to a low carbon, more resource efficient mode of operation. The accompanying Low Carbon Transition Plan¹³ confirmed world-leading long term emissions reduction targets (a legally binding commitment to cut by 80% by 2050), a set of Carbon Budgets¹⁴ for Government to help keep the UK on track, and a wide-ranging package of policies to drive the change.

11 It could build quickly on existing standards work in this space, including the Publicly Available Specification (PAS) 2050 on measuring embodied emissions in goods and services, the intended PAS 2060 on carbon neutrality, and follow up to the recent strategic review by BSI of standards for resource and waste management.

12 <http://www.berr.gov.uk/files/file52002.pdf>

13 http://www.decc.gov.uk/en/content/cms/publications/lc_trans_plan/lc_trans_plan.aspx

14 With a milestone target of an 18% reduction on 2008 emissions levels by 2020.

3.10 The EU Emissions Trading Scheme,¹⁵ which implements carbon pricing and the forthcoming CRC Energy Efficiency Scheme,¹⁶ are lead policies driving emissions reductions in business. There is a policy framework – the Waste Strategy and the recent Statement on Policy Aims for Commercial and Industrial Waste¹⁷ – and a key economic instrument – the Landfill Tax – to encourage more sustainable waste management, away from landfill, towards material resource and energy recovery.

3.11 Government provides support and information to business on the opportunities of resource efficiency and low carbon via a “one stop shop”, now led by the Waste Resource Action Programme,¹⁸ which is accessible via a web portal.¹⁹ The Carbon Trust²⁰ helps business become more energy efficient; and the Government published “Can you afford not to?” a guide to opportunities in low carbon and resource efficiency for businesses²¹ last autumn.

3.12 Infrastructure UK, the advisory body established by the Government last summer to advise on the country’s long term infrastructure needs, is developing a strategy which will identify the major challenges associated with developing infrastructure and will make recommendations for action. In addition, the Government published a Policy Statement on Regional Strategies on 23 February 2010²² to bring together economic development

15 http://www.decc.gov.uk/en/content/cms/what_we_do/change_energy/tackling_clima/emissions/emissions.aspx

16 http://www.decc.gov.uk/en/content/cms/what_we_do/lc_uk/crc/crc.aspx

17 <http://www.defra.gov.uk/ENVIRONMENT/waste/topics/index.htm>

18 <http://www.wrap.org.uk/>

19 http://www.businesslink.gov.uk/bdotg/action/detail?type=ONE_OFFPAGE&itemId=1082105198

20 <http://www.carbontrust.co.uk/>

21 http://www.businesslink.gov.uk/Horizontal_Services_files/business_success_low_carbon_economy.pdf

22 www.communities.gov.uk/publications/planningandbuilding/policystatementregionstrat

and spatial planning, enabling a joined up approach to economic, environmental, housing, employment and transport policies.²³ It puts in place a new approach for the Regional Development Agencies, requiring them to join up national and regional priorities and consider the impacts of their investments at national as well as regional levels. The Government will work with the RDAs to encourage this new approach and will drive alignment at national, regional and local levels.

3.13 The Government has already signalled its priority on engaging coalitions of employers more effectively with development of skills for different areas of the low carbon economy, e.g. for the new Low Carbon Economic Areas. The National Skills Strategy last autumn reported work underway to deliver an analysis of skills needs for the growing renewable energy sector.²⁴ The Government will consult further on its strategy for low carbon skills this Spring.

Priority actions for Government:

1. **Infrastructure:** Government will work with the RDAs to ensure a strategic approach to development of low carbon, resource efficiency infrastructure in regional economic planning.
2. **Market framework:** BIS should work with Defra, DECC, BSI British Standards, business and others towards the strategic objective of defining a clear standards and measurement framework for business to use in a low carbon, resource efficient economy.
3. **Capability:** The Government should continue to raise awareness of the business benefits from improving resource efficiency and new innovative approaches through, for example, WRAP, Business Link and the Environmental Sustainability Knowledge Transfer Network and, in consultation with business and others, develop further its strategic approach to low carbon skills needs across the economy.

²³ The economic priorities underpinning this approach were set out in Partnerships for Growth: A National Framework for Regional and Economic Development, <http://www.berr.gov.uk/files/file53941.pdf>, published in December 2009, which defined a single set of strategic priorities for sustainable economic development at national, regional and local level. Partnerships for Growth sets out these priorities for policies such as skills, innovation, infrastructure and finance, and for support to key sectors such as low carbon industries, life sciences, creative and digital industries, and advanced manufacturing.

²⁴ The National Skills Strategy, November 2009, <http://bis.gov.uk/policies/further-education-skills/skills-for-growth>

4: Globalisation and business services

4.1 The evolution of business services in the UK needs to be seen in the context of the dramatic changes in the global economy over the last three decades. At the heart of this was the acceleration in the pace of globalisation, with world trade in goods and services increasing more than sevenfold since the 1980s.

4.2 These trends have been driven not just by the advanced economies but also emerging countries, whose share of world trade has more than quadrupled. The integration of the latter into global markets has also underpinned a fourfold increase in the effective global supply of labour, primarily in the form of low skilled workers.

An edge in exports

4.3 This trend is expected to continue, with China and India alone expected to add over 300 million workers to the global labour pool by 2030. In the medium term, their comparative advantage will remain in low to medium skill activities. Figure 3 below shows the revealed comparative advantage for professional and business service (part of other business services) and others when compared with emerging economies.

4.4 Key to unlocking the potential of overseas markets has been developments in ICT and Logistics. These have made it possible to split out

and separate particular production activities,²⁵ or remotely deliver services which would have previously required face to face contact. This has encouraged increased outsourcing of certain activities to specialist providers with global reach and expertise.²⁶

4.5 However, it is clear that the ambition of the new emerging economies is not simply to remain as a source of low cost manufacturing but rather to develop the capacity to move up the value chain in both products and services: from “Made in China” to “Designed in China”.

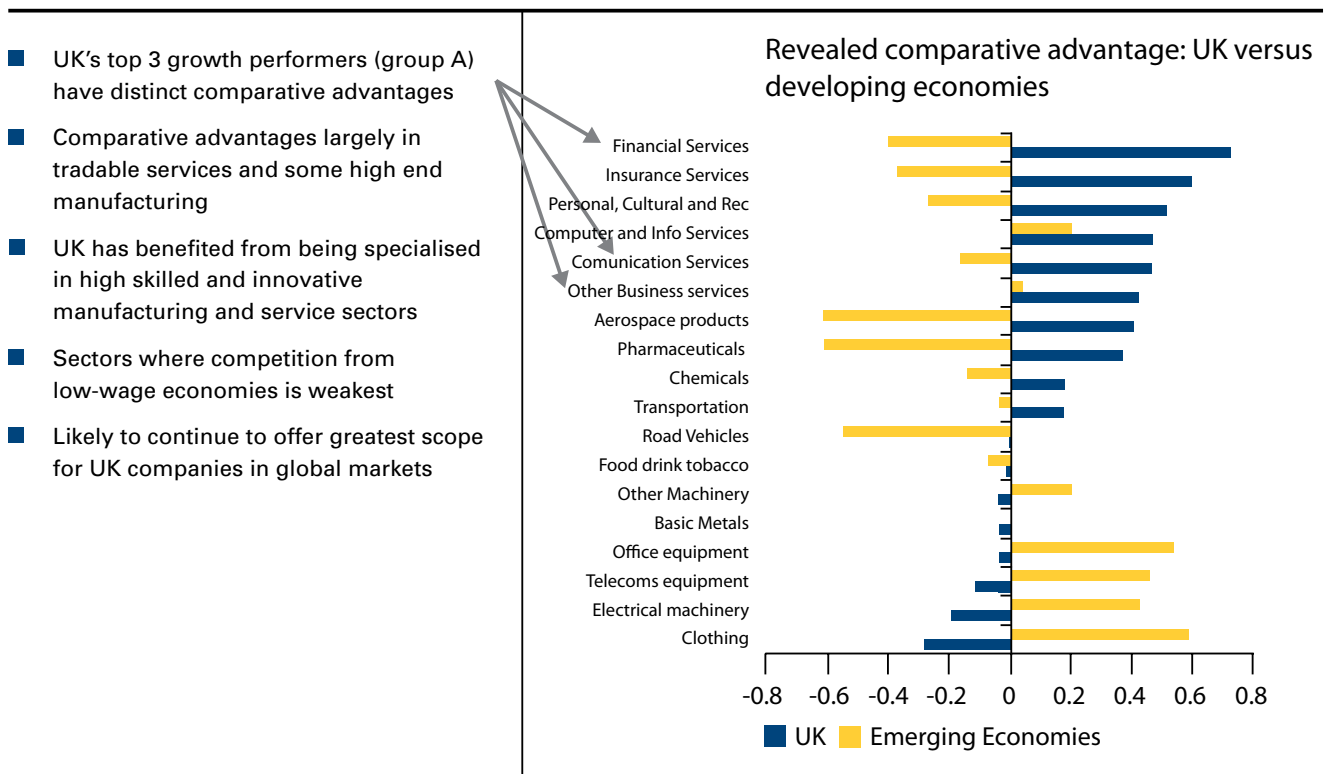
4.6 But, as the “New Industry, New Jobs” report²⁷ indicated, the growth of the emerging economies provides significant opportunities for innovative firms: Demand for services is proportionately higher among the global middle class and the increase in this socio economic group will derive almost exclusively from the developing world.

4.7 The UK’s competitive advantage is not simply in relation to the emerging economies. The UK is the second largest exporter of business services after the USA and economic analysis of revealed comparative advantage indicates that the UK enjoys a clear comparative advantage in

25 World trade in intermediate products grew five-fold between 1988 and 2006, WTO (2008)

26 See STI (2007), BERR (2009) for a more detailed discussion of the theory and evidence.

27 New Industry New Jobs April 2009

Figure 3 Symmetric revealed comparative advantage – emerging economies

most areas of business services compared to our major G7 competitors (see Figure 4 below).

4.8 Increased globalisation has led to fears of UK service jobs going overseas. However, despite being one of the largest off-shorers of business services in the G7, the UK actually on-shores substantially more of them. Indeed, overall, the UK is the largest net exporter of business services in the G7.²⁸

UK capability

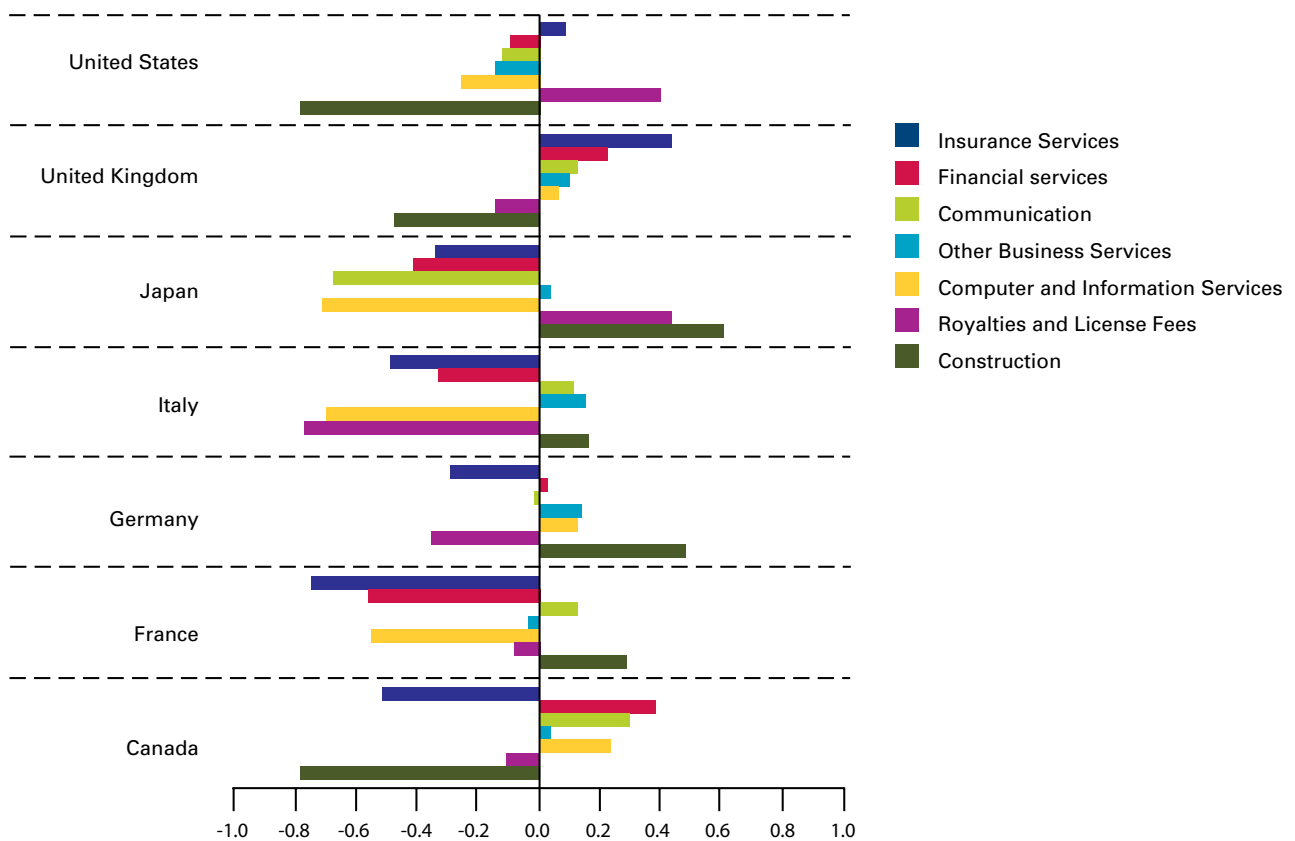
4.9 The UK has a global reputation in developing creative solutions to complex problems and providing a reliable means for resolving disputes. It has also developed a reputation for developing business information services, branding, advertising and corporate communication in a world where intangible assets have become critical to business success.

- As Government organisations in both developing and advanced economies seek to provide innovative and cost effective solutions to public service delivery, the experience of Public Private Partnership and Private Finance Initiative approaches to the delivery of public sector infrastructure and service projects in the UK has enabled UK firms to exploit their knowledge and gain public sector contracts worldwide.

- English Common law is frequently used to govern international commercial contracts and, as a result, English lawyers and English courts are often used to resolve disputes arising from these contracts. Even where English law is not used in a contract, the commercial court in London may be used to resolve disputes because of the excellent reputation of the English judiciary and the profession for expertise and impartiality. High quality arbitrators and mediators are also far

28 See also Amti and Wei (2004).

Figure 4 Symmetric revealed comparative advantage- G7 UK capability



Source: OECD Trade in Services Database

more widely available in the UK than in US and 98% of alternative dispute resolution is UK based.

- Global firms, from the USA as well as a wide range of European, Middle East and Asian organisations, source their corporate communications projects in the UK;
- Thomson Reuters, Pearson and Reed Elsevier are leading companies in the field of business information/workflow;

Business priorities for Government

4.10 In our Consultation with business particular emphasis was given to the following:

- The sheer scale of opportunity for business services in the area of services related to sustainability and infrastructure. For example,

the OECD estimates that almost \$2 trillion pa will need to be spent on transport infrastructure, telecommunications, electricity and water in the period to 2020, at a time when financial resources are constrained and innovative approaches to project funding will be required.

- The growth of competition from the emerging economies of India and China, as they developed the skills and capabilities to offer ever stronger services in established market areas, e.g. offshore software, construction and verification services.

- UK providers being pushed towards specialisation and more focus on strengths in high value services with a high degree of customer interface requiring “soft skills”, and in managing large integrated service offerings

and project management. For example, where power companies pitched alongside carbon market services to offer generation capacity and the associated carbon measurement and verification services.

- The need for Government to develop targeted programmes in leading emerging economies, over the next three years, which played to the needs of the host country.

- The intensity of competition from other G7 economies and their perception that other Governments did more to champion exports of business services than the UK authorities.

Government strategy

Inward investment

4.11 The UK has attracted a considerable flow of inward investment as firms seek to tap into the professional and business service

The UK: a global hub for the international carbon market

The City of London is the global hub for the international carbon market. Several hundred companies offer services around the frameworks of the EU Emissions Trading System and the Kyoto Protocol. These encompass specialist consultancies, lawyers, emissions auditors, carbon brokers and project developers. This activity has grown rapidly over the last decade, driven by the introduction of legislation to tackle climate change and trade carbon. In 2008 the global market was worth \$125 billion, twice its value in 2007. More recently, the economic downturn and the outcome of the Copenhagen summit both slowed market investment, but the sector is expected to grow again by 2020.

The business perspective is that international carbon markets will grow in the medium term despite the uncertainties flowing from the failure at Copenhagen to set a timetable for a legally binding international climate change agreement for post-2012. This growth will be shaped by both national and international regulation and development of emissions trading systems; the potential emergence of the US as a carbon market hub³⁰ will be a major factor. Business thought a system of trading schemes, perhaps linked, was likely by 2020.

Carbon market businesses wanted to strengthen their dialogue with Government with the twin aims of maximising the UK share of global carbon markets and developing further the world-leading capabilities of the London market hub in the face of the initial market uncertainty post-Copenhagen and prospective challenges from competitor centres in the US and Far East. Ambitious climate change legislation and targets were needed to drive growth in the carbon market services sector.

Carbon market companies in the UK are currently supported and promoted by the Climate Change Projects Office (CCPO) – a joint BIS-DECC office. CCPO runs trade missions with UK Trade & Investment that facilitate business for the sector; it advises companies on opportunities, and feeds in practical market experience to policy debates.

29 The US is currently considering the introduction of a cap and trade scheme which would significantly drive demand for carbon market services.

sector's expertise. Chapter 1 emphasised the clustering of this activity in London and the South East. This is particularly pronounced in relation to specific sectors, such as legal services, accountancy, branding and corporate communications, and in relation to carbon trading and management services, where London is a world-leading hub which serves the growing international carbon markets. The combination of talent and business environment has made the UK an attractive location for business service firms and Chapter 5 considers the key elements of the business environment which need to be addressed to maintain this position as a global hub for business services.

Opening markets in Europe and beyond

4.12 In many instances around the world, opportunities for UK business services providers, and the contribution that they could make to local economic development, are restricted by regulatory barriers to trade which prevent them from participating fully in overseas markets. Barriers may take the form of explicit constraint on foreign participation in national markets or discriminatory application of administrative processes such as licensing. Many sectors and markets are affected in this way; for example, the provision of satellite services in Argentina, telecommunications services in Brazil, postal services in Canada and China, insurance services in Japan and retail in India and Thailand.

4.13 The UK Government has been successful in including market access issues of importance to UK businesses in the EU's Market Access Strategy. In addition, UKTI's Joint Economic and Trade Conferences pursue issues with external markets. BIS aims to ensure that business and professional services remain priorities in the

World Trade Organisation and bilateral trade negotiations.

4.14 Within Europe, business services have received increasing attention in EU policy making, and the UK promoted these sectors in the strategy paper "The Future of EU Competitiveness"³⁰ published last summer. The EU Services Directive makes it easier to export a range of services within the EU. BIS is providing advice and guidance to business on the opportunities³¹. The Government has advised the European Commission that the UK supports a focus on business and professional services in the assessment of the impact of the Directive across EU Member State markets.

4.15 It is also working collaboratively with other member states and DG Enterprise on the EPISIS project, to foster a shared understanding of the policy measures required to promote innovation in services and their internationalisation. Notwithstanding the efforts to promote a single market for services, cultural barriers often deter or prevent SMEs from tackling European opportunities. The success of EU academic mobility programmes has prompted the UK to propose a pan-European SME secondments programme, linked to venture capital networks, and is working with the Commission to see how to turn this into a reality for innovative SMEs.

Championing exports of business services

4.16 Since launching the Chancellor's City Strategy in 2006, UKTI has already been working to transform the way it supports businesses exporting services from the financial and professional sector. UKTI has committed

30 <http://www.berr.gov.uk/files/file51732.pdf>

31 <http://www.bis.gov.uk/policies/europe/eu-services-directive>

additional resources to priority markets China, India and the US to work with UK firms, local governments and regulators to further the interests of UK businesses overseas in a co-ordinated marketing approach to increase export opportunities. It is driving forward a UK Low Carbon International Marketing Strategy³² in partnership with business to support UK suppliers of environmental goods and services in this critical, high growth area of the global market.

4.17 UKTI is leading the UK Government's response to a recent approach from the Chinese authorities to set up a working group to look at opportunities for trade in the broad area of business services.

4.18 On export promotion of City-related professional services, UKTI is working with the business-led body "TheCity UK", to help ensure that it delivers the next step change in the promotion of UK financial and professional services overseas. UKTI will support TheCityUK

aim of establishing a single strategic oversight of the UK's overseas promotional efforts, building on the work of UKTI to ensure that: overseas visits by Ministers, the Lord Mayor, the Mayor of London and senior industry figures continue to be co-ordinated as part of a long-term strategic plan; and that inward visits by senior industry and political figures are co-ordinated and targeted to benefit the UK.

Priority actions for Government:

1. UKTI will review with BIS, and in discussion with the business and professional services communities, what is needed to strengthen support for UK exporters of these services, and how best to meet these businesses' needs in priority overseas markets.
2. UKTI will continue to drive the UK Low Carbon International Marketing Strategy in partnership with business.
3. The DECC and BIS-sponsored Climate Change Projects Office should work with the UK's world-class carbon services industries to support its growth and opportunities across international carbon markets, including in the light of the post-Copenhagen uncertainties about international market development.
4. BIS will engage actively in European fora to promote the concept of service innovation in Europe. It will also review the scope for promoting to business the opportunities arising from implementation of the Services Directive and the EUGO network of Points of Single Contact across Europe.

³² <http://www.ukti-lowcarboneyconomy.org/>

5: A strategy for growth: strengthening the business environment

5.1 Our analysis suggests that globalisation, the challenge of sustainability and technology development will bring about a measure of structural change to all sectors. Clearly, those sectors which are most susceptible to developments in digital technology, eg advertising and digital content services, will face the greatest disruption – and the greatest opportunity – while business service firms engaged in sectors associated with climate change and sustainability have opportunities for growth, albeit over an uncertain timescale. Previous chapters have set out business priorities for Government action in terms of infrastructure, a clear market framework, and strengthening UK capability through access to technology and improvements in skills.

5.2 But even the more traditional professional services face change. For the most part, growth within the UK is likely to remain closely tied to the business cycle and investor confidence. However, over the next five to ten years, competition in legal services will intensify as new legislation permitting incorporation comes into force: less complex legal advice, or activities which can be standardised, will either be outsourced to low cost operations or even succumb to a degree of automation. High value activities will also come under pressure as other locations, such as Frankfurt, Geneva and Singapore compete with London as a hub of legal expertise in specific areas eg finance or shipping. Professional firms, unable

to demonstrate innovation and success, will struggle in a more competitive climate, but organisations (or individuals) with particular expertise and high customer standing will continue to prosper.

5.3 In developing a growth strategy for this sector, business urged Government to strengthen the UK's attractiveness as an HQ for European and Global business and, more broadly, as a hub for innovative service firms. In so doing, business has indicated that Government should learn from the earlier success.

5.4 In the UK, past success in professional and business services has been driven by a number of factors which included the following:

- A tradition of speedy resolution of disputes and fair effective restitution, together with high standards of accounting and financial reporting;
- A broad business environment which encouraged competition, enterprise, problem solving and risk taking, as well as a strong appreciation of the importance of design and marketing as drivers of value added;
- A regulatory regime which fostered the development of London as a global hub of financial services that, in turn, acted as a

beacon for the best UK and global talent and supported extensive development and regeneration in and around the City;

- A trend towards the outsourcing of activities, not least by public services, which now account for some £80 billion of economic activity, or 6% of GDP; and
- A recognition that competitive advantage in manufacturing lay, not only in the functionality and performance of the product, but also in intangible aspects associated with it, including brand image, service support and financing, which has increased trade in high value services as global firms have sought UK expertise.

5.5 The rest of this chapter focuses on a number of horizontal policies measures, that the government is using to strengthen the business environment and which also have particular relevance to the professional and business services sector.

Finance

5.6 The challenges faced by the banking sector and the global economic downturn had a negative impact on the banks' ability to fund themselves and Governments world wide have taken a range of measures to restore stability and liquidity to capital markets and ensure the availability of finance for business.

5.7 However, even before the downturn, the ability of some business requiring access to finance was significantly affected by market failures. Research shows that start ups and young businesses, in particular, consistently experience greater difficulties in accessing

finance.³³ As one might expect, the uncertain economic environment did not help matters. Nevertheless, the majority of SMEs are still able to obtain at least some of the finance they need with approximately 78% of SMEs doing so from the first source they approached.³⁴

5.8 The Government has continued to encourage banks to lend under normal commercial terms to those with viable business plans. However, for those without significant security or credit history, otherwise viable businesses at the margins of commercial decisions, the government has intervened through the Small Firms Loan Guarantee Scheme and now through the Enterprise Finance Guarantee Scheme³⁵ To date, the Enterprise Finance Guarantee (EFG) has been offered to nearly 8,100 businesses, with loans totalling nearly £826m. EFG has been extended until March 2011, thereby supporting businesses in gaining sufficient access to finance as we return to economic growth.

5.9 It is also necessary to consider the availability of equity finance to SMEs. Although only a small proportion of SMEs seek equity finance (1-2% of those seeking finance), it is especially important for young and innovative businesses with high growth potential. Research³⁶ shows the continued existence of an "equity gap" for viable SMEs seeking equity finance. The upper boundaries of the gap have increased in recent years for the majority of SMEs seeking

33 BERR (2007) Annual Small Business Survey 2006/07

34 The BIS 2009 finance survey shows that 78% of SMEs who sought financing obtained some finance from the first source approached.

35 Up to £1.3 billion of new bank lending is being guaranteed by the Government since launch in January 2009 up until 31 March 2010. Up to £500 million of new bank lending will be guaranteed between 1 April 2010 and 31 March 2011. Businesses in the UK with an annual turnover of up to £25 million are eligible to borrow between £1,000 and £1,000,000 when this would not otherwise have been possible.

36 The supply of equity finance to SMEs: Revisiting the Equity gap

equity finance to between £2m to £10m³⁷. The government has a range of equity schemes including Enterprise Capital Funds providing equity finance to viable SMEs seeking finance in the equity gap.

5.10 Our consultation with business indicated that access to angel finance is a key issue and this is covered below under taxation.

Taxation

5.11 Tax can play an important role in supporting the overall business environment. The UK provides a competitive tax regime for businesses, with the corporation tax rate of 28% the lowest among G7 countries, and the lowest ever in the UK, alongside a tax rate for small companies that is low by international standards. The tax system also provides generous reliefs targeted at specific market failures, such as improving access to finance for small and growing businesses. However, in our consultation for this report, business raised concerns about the reforms to capital gains tax (CGT) in 2008, in particular the impact on financing start-up businesses of removing CGT taper relief. On 22 February, HM Treasury published a draft Framework for Business Taxation.

5.12 The Government is seeking feedback on the draft, which sets out:

- The key principles underpinning the development of tax policy – including securing fairness, competitiveness and stability for the UK, and ensuring new burdens and complexities are not created for UK business

- The policy process the Government follows when developing tax policy, including consultation wherever possible.

Regulation

5.13 The UK is the easiest place to set up and run a business in Europe: The World Bank found that it takes 13 days to set up a business in UK, compared to the European average of 15 days. It ranks the UK first in Europe and fifth in the world to operate a business³⁸.

5.14 In our consultation for this report, business raised particular concerns in the area of employment law. It was also felt that complying with regulation is often more onerous for SMEs. The concerns raised echoed those made by the Institute of Directors *269 Regulatory Suggestions*, which Government responded to in October 2009.

5.15 Government will continue to look at all areas of regulation to find ways in which we can continue to simplify the requirements and reduce the costs falling on business, whilst meeting our overall policy objectives. In taking this work forward, we will ensure that the specific concerns of the professional and business service sector are addressed. In particular, we will ensure that regulation does not unduly hamper the competitiveness of the sector relative to international markets, as recommended in the Professional Services Global Competitiveness report published in March 2009.

5.16 Regulation is not just an issue for Government and this is particularly true with regard to professional and business services. The recent review of regulation by the Law Society

37 In 1998 one leading provider invested £908 million in 600 companies at an average investment size of £1.5 million. By 2007, it was investing £1.5 billion in 62 companies with an average investment size of £25 million.

38 Source: Doing Business 2010.

is an example of how seriously self regulation is taken by the professional bodies which represent the sector – see box below. Government will continue to work with the sector and representative bodies to ensure that future regulation is in line with maintaining overall competitiveness of the sector and the broader UK economy.

Review of regulation of legal services led by Lord Hunt of Wirral MBE

The legal sector is undergoing a radical transformation. Alternative Business Structures will have to be assimilated into the legal regulatory system, the ever changing demands of clients will need to be satisfied, and English and Welsh law must maintain the high international reputation which provides so many business benefits for the UK. For these, and many other reasons, it is critically important that the regulatory system is constantly reevaluated to ensure it is fit to meet both new challenges, and long standing regulatory needs.

Employment and Skills

5.17 Business emphasised the importance of investment in skills to support future growth and performance in business and professional services, including the management and technical capabilities to deliver in response to the fast-moving demands of globalised service markets.

5.18 Our consultation with business indicated:

- The premium they placed on skills sets, such as organisation and project management, an understanding of changing business

models, creativity and initiative, as well as harder technological skills, such as ICT. It is this combination of so called “soft” and “hard” skills which provides the management *agility* required to flourish in business service markets. Components of this included: a good understanding of the opportunities of globalisation; the ability to develop and work in a cross-disciplinary mode to deliver service offerings; and an understanding of engineered services;

- The need to develop specific expertise, to meet new market demands and challenges, such as the call for accountants and lawyers to understand the essentials of carbon reporting; and
- A perception that the academic world did not appreciate the importance and changing nature of business services. Whilst there were strong patterns of recruitment between some business service sectors, such as the professions, and higher education, this was not so in many other sectors.

5.19 The Government has recently published a National Skills Strategy and Higher Ambitions setting out between them the policy framework for skills development and the contribution of further education towards economic growth.

5.20 BIS will engage with trade associations and Sector Skills Councils to explore the scope to broker stronger engagement between leading business services providers and the higher education sector in the UK.

5.21 Business also raised the importance to the UK’s service sectors of access to the global talent pool and the flexibility to bring world class staff

to this country in order to boost UK-based firms' abilities to tailor and deliver the best possible service solutions in the UK and wider global marketplace. Current UK migration policy was seen by some as an impediment to this. BIS recognises the importance of this issue and is working closely with Home Office to ensure it is taken into account in developing and delivering migration policy, including strengthening the interface between the migration and skills system.

5.22 At the Global Investment Conference held on 22 February it was announced that the UK Border Agency (UKBA) will introduce a highly-trusted sponsor scheme for businesses in autumn 2010. This will mean that businesses that qualify as highly trusted will benefit from a more streamlined approach when bringing skilled workers to the UK. There will be reduced bureaucracy of sponsorship for these businesses, although the security of the border will not be compromised; a simpler process for changing licences and faster processing times will be introduced. We will base this highly-trusted scheme on that being introduced for educational establishments. UKBA will also be introducing a wider choice of foreign internship schemes, making it easier for businesses in the UK to bring over the brightest and best graduates from around the globe from spring 2010.

5.23 The Government plans to publish a UKCES Skills Audit, which will include an analysis of skills needs in the professional and business services sector and highlighted the significance of this sector for future economic growth. The Government will, at the same time, set out its response to the challenges raised in the Audit, including steps being taken to ensure better information is available to inform

choice, increase the supply of cross-economy skills needed for growth, support markets and sectors with strong growth potential, encourage employers to invest in high level skills, and monitor the progress of the system in delivering the skills we need.

Regional Development

5.24 The Government published a Policy Statement on Regional Strategies on 23 February. This brings together economic development and spatial planning, enabling a joined up approach to economic, environmental, housing, employment and transport policies to:

- Align public and private sector investment around the delivery of a common set of agreed objectives.
- Drive the development of low carbon and sustainable regional, sub-regional and local economies and support them in responding to changing economic conditions whilst also protecting and enhancing the environment and the well-being of communities.
- Set out regionally and, where appropriate, sub-regionally specific policies which focus on key priorities, and provide a clear framework for local decision makers and public and private investors.
- Secure a joined up approach to strategy-making and governance within each region, based on partnership working and stakeholder involvement.

5.25 The economic priorities underpinning this approach were set out in Partnerships for Growth: A National Framework for Regional and Economic Development. This was published

in December 2009 following the commitment in New Industries, New Jobs, published in April 2009. Partnerships for Growth puts in place a new structure for the Regional Development Agencies, requiring them to join up national and regional priorities and consider the impacts of their investments at national as well as regional levels around key sectors and policies such as skills, innovation, finance and infrastructure. Government will work with the RDAs to ensure the regional dimensions of professional and business services are fully exploited, which includes maintaining London and the South East as a global hub, driving performance across the wider economy, and delivering the transition to a more networked low carbon society.

Public Procurement

5.26 Government itself has played an important role in fostering innovation and growth by being open to using new delivery methods for public services, such as greater use of the private sector. The Public Service Industry now accounts for around 6% of GDP and, in many cases, has been instrumental in generating innovative new approaches to service delivery. However, an independent review on the Public Service Industry prepared for the Department in 2008, under the Chairmanship of DeAnne Julius, identified the scope for improvements in the way services were procured. The Government has made considerable progress in implementing the main recommendations – see Annex.

5.27 Business, however, considers that the growing threat to frontline services, in the face of constraints on public expenditure, requires a further shift towards opening up public services to competition and the possibility of “public service process re-engineering”. Service providers point to the progress made by local Government in this regard and believe that services provided by central Government could benefit from a more radical approach to contestability. To promote such a strategic discussion and better procurement practice, we have committed to developing a constructive dialogue between departments and the business services sector, to identify good practice, monitor progress and the scope for improvement.

Responding to this interim report

This interim report has set out the key challenges and opportunities facing the professional and business services sector over the next ten years, and has been based on extensive consultation with the sector. It has also set out what Government is currently doing to support the sector and priorities for future action.

The aim is to establish the right priorities for Government action and to arrive at policy recommendations which will help to ensure the future success of the sector, whilst maximising its wider contribution to the UK's performance and growth. We want to check with business that we have got it right, and that is why this is an interim report.

The 22 March 2010 Professional and Business Conference: A 2020 Vision for Growth, will be used to debate the interim report findings. The final report will be published in the summer.

The Department for Business, Innovation and Skills has established a Services Policy Unit to act as a key point of contact for the industry. To find out more, contact:

Tel: Chris Tollady on +44 (0)207 215 1672

Email: chris.tollady@bis.gsi.gov.uk

Web: <http://www.bis.gov.uk/Policies/business-sectors/innovation-in-services>

Annex

Response: Public Services Industry Review

The Public Services Industry (PSI) Review was published in July 2008. It focused on defining and estimating the size and growth of outsourced services by the public sector; establishing the rationale for, and understanding the barriers to, effective outsourcing; the scope for exporting UK expertise; and it presented a vision of the future. It made eight recommendations and this section summarises the Government's approach and the progress being made:

1. Long term commitment. The Department is working with the Office of Government Commerce (OGC) to develop and publish a set of principles for public procurement and the way the government interacts with the supply markets on which it depends. The principles include the provision to industry of clear, timely information on future needs.

2. Clear and consistent objectives. OGC leads a cross-government commissioning group to promote and develop good commissioning practice, including where appropriate the use of outcome- and output-based procurement. The OGC/BIS publication *Driving Innovation through Public Procurement* similarly promotes use of outcome- and output-based specifications where appropriate; there is a link to OGC guidance on when to use outcome, output and input specifications. Outcome-based specifications feature in Departments' Innovation Procurement Plans.

OGC has issued clear guidance on how to cater for environmental and social issues in procurement, and is soon to publish an assessment tool showing procurers which Policy through Procurement agenda(s) is/are likely to be relevant to what they are buying. Although there are upwards of a dozen agendas that may apply on a case-by-case basis, the government has decided to focus on three as priorities: enabling SME and 3rd sector access to procurement; apprenticeships, training and youth employment; and carbon reduction. These priorities will be supported and monitored centrally and suppliers' support will be enlisted on a voluntary basis.

3. Competitive neutrality. Barriers vary widely across public service markets, and tackling these requires a detailed, service-specific review of the issues in each public service market. We consider Departments should continue to be responsible for identifying and tackling the issues where they arise.

HM Treasury supports commissioners by providing guidance on how to consider tax treatment when comparing bidders from different sectors – private, public and third sector. For example, on VAT, the Government's policy is that unjustified VAT obstacles to the development of competitive markets should be avoided. The key principle is consistency of treatment. This means that if differentials in the VAT treatment of providers are unavoidable, commissioners should identify the differences

and use notional comparators to evaluate all bidders as if the same tax treatment were applied to all.

The Government recognises that the inability of charities to recover VAT on non-business and exempt activities can be seen as an obstacle to the third sector taking a greater role in public service delivery. However, following two recent reviews, the Government rejected establishing a refund scheme for charities on grounds of both principle and cost.

Rather than make special VAT refund arrangements for public service delivery, HM Treasury encourages service funders to fund service providers' overhead costs – including irrecoverable VAT – within the contract price for a service, through 'Full Cost Recovery' and 'Guidance for Funders'³⁹.

4. Partnerships. As the report indicated partnerships are particularly important in the delivery of complex services over a long period. In 2009 OGC published a guide on the management of complex and longer-term contracts which emphasises the need for effective, structured relationships between authority and supplier.

5. Commissioning skills. In its White Paper, "Putting the frontline first: smarter government" the Government has indicated that it will strengthen procurement capability, by building on the OGC's work and publishing a second wave of Procurement Capability Reviews. It will also ensure that each department has a Director responsible for service delivery. This Director could originate from the commercial function or

work alongside the commercial function to make the improvements in contract development and management outlined in the PSI Review.

6. Bid costs. OGC has been working closely with industry to develop a broad range of standard contracting model templates and tools for public sector procurers. They aim to help reduce both the timescales in the procurement process and expenditure on external advisers, and also achieve a more consistent approach to public sector contracting, leading to efficiencies in tendering costs for all parties. These tools include: a new standard pre-Qualification Questionnaire for low value procurements, a suite of model contracts, and a new procurement timelines tool that emphasises the need for effective pre procurement supplier engagement and planning in order to reduce the overall timescales of a procurement process.

7. Raising the profile of the PSI internationally. The Government shares the view there are opportunities for the UK PSI to develop business overseas on the basis of its strong reputation for innovative delivery of public services in the UK. Some important PSI companies are already active in important markets.

UKTI has taken the following action to promote the UK PSI internationally, in partnership with the bodies representing the sector:

- a. It is Involving PSI companies in UKTI's work under the UK International Marketing Strategy for Financial Services. In partnership with IFSL British Expertise and CBI, UKTI has prepared new marketing material to promote

³⁹ <http://www.hm-treasury.gov.uk/media/9/4/guidncefunders1505061v1.pdf>

UK excellence in delivering high quality public services by leveraging private sector expertise in innovative ways (PPP, PFI & PSI). .

long term facilitate greater trade and investment between the UK and its trade partners.

- b. It is working with trade bodies representing the sector to ensure they are fully aware of the UKTI services available to PSI companies. Some companies, including Serco already make use of these services which include:
- i. The Overseas Market Introduction Service through which companies can commission for a small fee bespoke research into market opportunities, contacts and networks. The work is undertaken for customers by UKTI teams in British Embassies, High Commissions and Consulates overseas and usually commissioned through UKTI international trade advisers (ITAs) in the region⁴⁰;
 - ii. Sectoral marketing events in the UK and missions overseas where companies can meet overseas procurers and other contacts. The key sectors of interest include ICT, healthcare, infrastructure, service industries, defence and security. The purpose of such events is to market UK strengths in a consistent manner, increase awareness of skills and expertise in the sector concerned, enabling companies to lever the UK's reputation to develop their own business;
 - iii. Political support or lobbying to influence policies that remove barriers to market entry by overseas companies and in the

8. Engagement with the PSI. To promote better procurement practice, we have committed to developing a constructive dialogue between departments and the business services sector, to monitor progress and the scope for improvement.

⁴⁰ ITAs are accessible via the search facility on the homepage of the UKTI web portal www.uktitradeinvest.gov.uk



Printed in the UK on recycled paper containing a minimum of 75% post consumer waste.

Department for Business, Innovation & Skills. www.bis.gov.uk

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